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407 South Dearborn Ave.  
Suite 550  
Chicago, Illinois 60605  
Phone 312/427-8070  
Fax 312/427-4007  
woodstock@woodstockinst.org  
www.woodstockinst.org

March 26, 2004

Ms. Jennifer J. Johnson

Secretary

Board of Governors of the Federal Reserve System  
20th Street and Constitution Avenue, NW  
Washington, DC 20551

Re: **Docket No. R-1181**

Dear Ms. Johnson:

I am writing from Woodstock Institute in Chicago to comment on the **proposed** changes to the regulation of the Community Reinvestment Act (CRA). Woodstock Institute is a Chicago-based nonprofit research and advocacy group that has focused **on** community reinvestment policy for over 30 years. We feel that **the** proposed changes to the CRA regulation will significantly roll back policy essential for **community** reinvestment **and** misses a critical opportunity to close loopholes and modernize the **CRA** regulation.

### Small Bank Limits

The proposed **CRA** regulation would change the definition of "small bank" from any institution with less **that** \$250 million in assets and not part of a holding company **with** over \$1 billion in **assets** to include **all** institutions with less **than** \$500 million in assets regardless of holding company size. This change **will** dramatically increase the number of **banks** considered "small" **that, for** CRA purposes, are **not** examined for their levels of **community** investment **and** services under the streamlined **small bank CRA** examination. This **will** disproportionately effect **rural** communities **and** small cities **where** **smaller** institutions have significant market **share**. In Illinois, **it** will reduce **the** number of institutions covered **by the** comprehensive CRA examination **by 63** percent, **from** 198 banks to **74**. However in rural areas or small **cities**, the number of institutions covered by comprehensive CRA will decline by nearly **73** percent.' In **these** communities, already struggling, **banks** will **be** less compelled to provide innovative investment opportunities **and** services. Additionally, these banks will no longer be required to report **small business lending data**. **This will** significantly reduce available data on small business lending despite the fact that it has been shown that **small banks** have a **larger** share of their lending dedicated to small businesses than larger banks.

Another concern is that by removing **the** holding company threshold from the definition of small bank, regulators **will** not only reduce the **number of** institutions covered by comprehensive CRA, but also have created a potential loophole for large holding companies to exploit when trying to evade CRA compliance. **This** change raises the **possibility** that large holding companies **will re-form** their banking subsidiaries **as a** series of local "small banks" to avoid comprehensive CRA examinations. In the Chicago area, such **an** institution already exists. Harris Trust **and** Savings currently **has** **26** separately

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chartered institutions in the Chicago area totaling over \$30 billion in assets. Of these institutions, 19 would be considered "small" under the **new CRA** regulation despite being part of Bancmont Financial Corp, a holding company with over \$39 billion in **assets** in the United **States**. Of those Harris institutions not covered, **a** least three serve communities with significant low-income or minority populations.<sup>2</sup> Although **we** do not feel that Harris has structured its holding company to evade CRA compliance, **we** feel that holding companies could use this structure as a model to avoid significant compliance with CRA.

Woodstock feels expanding the definition of "small bank" disproportionately harms rural communities and creates a loophole for larger financial institutions to exploit in getting around **full** CRA compliance.

### **Affiliate Lending and Assessment Areas**

Regulators missed a significant opportunity to **modernize** CRA by not requiring affiliate lending to be considered in CRA examinations. **As** bank holding companies increasingly use non-bank lenders to originate mortgages, it **is** critical that all lending affiliates be required to **report** lending in an institution's CRA examination. **As** currently structured, the CRA regulation allows banks to choose which **affiliate** loans in a given assessment area they **want to** apply toward the lending test. This **allows** institutions to cherry pick the best lending affiliates for each assessment area **and** exclude affiliates in assessment areas where those affiliates might not be adequately serving the community. **As** holding companies increasingly acquire non-bank lenders, **often** subprime lenders, it is critical that **this** loophole be closed and all lending affiliates be considered in CRA examinations.

Additionally, we were disappointed to see that **there** was no change to how assessment areas **are** considered. **As** technology and regulatory policy has advanced to allow financial institutions to conduct business through channels other **than** traditional branches, CRA has **not** advanced with it. **For** example, a recent Woodstock Institute publication illustrates that insurance banks conduct **over 75** percent of their lending outside of **their** CRA assessment areas.<sup>3</sup> To have this level of lending not fully considered in an institution's CRA examination gives banks another loophole to exploit in evading full **CRA** compliance.

### **Predatory Lending Standard**

**By** mirroring the OCC and setting a **weak** anti-predatory lending standard, regulators missed a significant opportunity to make a strong statement about predatory lending. The proposed standard allows that loans originated based on foreclosure value of collateral rather than borrower ability to repay can negatively affect a **bank's** CRA examination. This standard misses numerous predatory practices such **as** packing exorbitant fees onto mortgage loans, loan flipping, charging **high** prepayment penalties, **and** mandatory arbitration that can strip equity from homeowners and trap **borrowers** in

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<sup>2</sup>Harris Bank Argo, Harris Bank Westchester, and Harris Bank Aurora all serve minority or low-income communities.

<sup>3</sup>Katy Jacob, October 2003. *Reinvestment Alert 24: CRA, Financial Modernization and the Policy Implications of Insurance Company Involvement in Banking for Low-Income Populations*. Woodstock Institute, Chicago. Find at [www.woodstockinst.org/document/alert24.pdf](http://www.woodstockinst.org/document/alert24.pdf)

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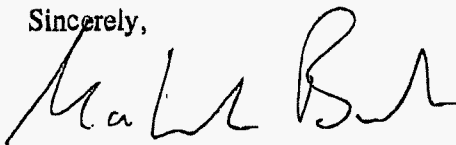
abusive loans. Regulators should apply a strong predatory lending standard to bank loans and to loans made by affiliates.

### Data Disclosure

We welcome additional data disclosures on CRA examinations, but feel the data need to be more fully considered in evaluations to be truly effective. Reporting the census tract location of an institution's small business loans will allow for greater understanding of how banks serve traditionally underserved communities. However, the benefit of this additional data is partly offset by loss of data for banks that would be considered "small" under new criteria. These lenders are significant providers of small business loans, and the loss of this data will create a significant gap in available data. Additionally, adding data to CRA examinations to differentiate between the share of bank and affiliate loans that are originated and purchased and those which are high interest rate and HOEPA loans is also a positive step, but these loans should not be weighted equally. Originated, lower interest rate, and non-HOEPA loans should be given more weight.

Woodstock Institute welcomes the additional data disclosures, but feels that proposed changes undermine the mission of community reinvestment by creating loopholes for financial institutions to exploit to evade significant CRA compliance. We also feel regulators missed a significant opportunity to modernize CRA to reflect the reality of how financial services are provided today. We urge you to reject the proposed changes to the definition of small banks; adopt a more inclusive policy toward affiliate lending and assessment areas; strengthen the proposed predatory lending standard; and maintain the data disclosure proposal.

Sincerely,



Malcolm Bush  
President

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